

## Message Text

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ACTION EUR-25

INFO OCT-01 ISO-00 SP-03 AID-20 EB-11 NSC-07 RSC-01

CIEP-03 TRSE-00 SS-20 STR-08 OMB-01 CEA-02 CIAE-00

COME-00 FRB-03 INR-11 NSAE-00 XMB-07 OPIC-12 LAB-06

SIL-01 SAJ-01 AGR-20 DODE-00 PA-04 USIA-15 PRS-01

DRC-01 /184 W

----- 020820

R 221426Z AUG 74

FM AMEMBASSY BONN

TO SECSTATE WASHDC 4558

INFO AMEMBASSY BRUSSELS

AMEMBASSY COPENHAGEN

AMEMBASSY DUBLIN

AMEMBASSY THE HAGUE

AMEMBASSY LONDON

AMEMBASSY LUXEMBOURG

AMEMBASSY PARIS

AMEMBASSY ROME

USMISSION EC BRUSSELS

USMISSION OECD PARIS

UNCLAS SECTION 01 OF 02 BONN 13285

DEPARTMENT PASS TREASURY AND FEDERAL RESERVE

E.O. 11652: N/A

TAGS: EFIN, ECON, GW

SUBJECT: THE FRG ECONOMY - THE FOOT NEARS THE  
ACCELERATOR

1. SUMMARY. THE BIGGEST QUESTION NOW IS HOW AND  
WHEN THE FEDERAL GOVERNMENT WILL STEP IN TO STIMULATE  
THE ECONOMY. THE CURRENT ECONOMIC SITUATION IN THE  
FRG IS MARKED BY LITTLE OR NO GROWTH, COMPARATIVELY  
HIGH UNEMPLOYMENT, AND MORE MODEST CONSUMER PRICE  
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INCREASES THAN PREVIOUSLY EXPECTED. THE GOVERNMENT



DENIES ANY INTENTION TO STEP ON THE ACCELERATOR AT THIS TIME, SUGGESTING THAT SUCH ACTION WOULD REDUCE THE SUCCESS OF THE GOVERNMENT'S CURRENT EFFORTS TO HOLD DOWN INFLATION. AT THE SAME TIME, HOWEVER, CONTINGENCY PROGRAMS ARE BEING PREPARED BY BOTH THE FEDERAL GOVERNMENT AND THE LAENDER GOVERNMENTS TO BOOST THE ECONOMY, PERHAPS IN THE FALL. IN THIS CONTEXT, CONSIDERATION WILL PROBABLY BE GIVEN TO USE OF THE DM 10 1/2 BILLION COUNTERCYCLICAL RESERVES HELD WITH THE BUNDESBANK. THE FOLLOWING OFFERS A PERSPECTIVE AND ANALYSIS ON UNDERLYING BUSINESS TRENDS AND CURRENT GOVERNMENT THINKING. END SUMMARY.

2. ACCORDING TO THE ECONOMICS MINISTRY, THE FRG IS MARKED BY LITTLE OR NO REAL GROWTH, WITH FOREIGN DEMAND THE ONLY SUSTAINING ELEMENT. THE UNDERLYING BUSINESS SITUATION, THE MINISTRY EXPLAINS, IS INFLUENCED TO A CONSIDERABLE EXTENT BY "STRUCTURAL ADJUSTMENTS" IN CERTAIN SECTORS TO UNFAVORABLE MARKET CONDITIONS. THIS APPLIES IN PARTICULAR TO THE BUILDING TRADE AND THE AUTOMOBILE INDUSTRY. THESE ADJUSTMENTS, THE MINISTRY ASSERTS, ARE LARGELY RESPONSIBLE FOR THE WEAKNESS OF THE LABOR MARKET. (NOTE: THE RATE OF UNEMPLOYMENT IN JULY--2.2 PERCENT IN ABSOLUTE TERMS AND 2.9 PERCENT ON A SEASONALLY ADJUSTED BASIS--IS UNUSUALLY HIGH BY GERMAN STANDARDS.)

3. THE MINISTRY ESTIMATES THAT REAL GNP DURING THE FIRST HALF OF THE YEAR EXCEEDED COMPARABLE 1973 LEVELS BY ONLY 1 - 1 1/2 PERCENT, AND IMPLIED THAT THIS GAIN WAS ACHIEVED PRIMARILY, OR EXCLUSIVELY DURING THE FIRST QUARTER. FOR THE SECOND HALF OF THE YEAR, THE MINISTRY ANTICIPATES AN ONLY SLIGHTLY HIGHER GROWTH RATE.

4. AT THE SAME TIME, THE MINISTRY NOTES SOME SUCCESS IN GRADUALLY CURTAILING CONSUMER PRICE INCREASES. DURING THE FIRST SEVEN MONTHS OF THE YEAR, THE COST-OF-LIVING INDEX AVERAGED 7.2 PERCENT ABOVE COMPARABLE 1973 LEVELS, I.E., NOTABLY LESS THAN PREVIOUSLY

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ANTICIPATED. ACCORDING TO THE MINISTRY, THIS RATE WILL PROBABLY RISE IN AUGUST AND SEPTEMBER, BUUT THE



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FOURTH QUARTER IS LIKELY TO BRING RENEWED DECELERATION.  
THE YEAR-TO-YEAR RISE OF LIVING COSTS IN 1974 AS A  
WHOLE IS PLACED AT A MAXIMUM OF 7 1/2 PERCENT, A  
MODEST INCREASE IN LIGHT OF ANTICIPATED DEVELOPMENTS  
IN OTHER NATIONS.

5. DESPITE SLOW GROWTH AND RELATIVELY HIGH UNEMPLOYMENT,  
THE GOVERNMENT OSTENSIBLY REJECTS REFLATION AT THIS  
POINT. IN AN INTERVIEW WITH DER SPIEGEL (TRANSLATION  
TO FOLLOW IN AIRGRAM), CHANCELLOR SCHMIDT ASSERTED  
THAT THE CURRENT SITUATION DOES NOT WARRANT SUCH A  
MOVE, FOR "WE DO NOT WANT RENEWED ACCELERATION OF  
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PRICES." HE ALSO REJECTED GOVERNMENT SUPPORT FOR THE AUTOMOBILE AND CONSTRUCTION INDUSTRIES. IN HIS VIEW, THE REDUCED DOMESTIC DEMAND FOR AUTOMOBILES RESULTS FROM CONSUMER RESTRAINT IN THE FACE OF THE OIL PRICE EXPLOSION. HE NOTED THAT THE PROBLEMS OF GERMAN AUTOMOBILE PRODUCERS WERE INEVITABLE AND SIMILAR PROBLEMS ARE FACED BY PRODUCERS ELSEWHERE IN THE WESTERN WORLD. REGARDING THE BUILDING TRADE, THE CHANCELLOR OBSERVED THAT A REDUCTION IN PRODUCTIVE CAPACITY IS NOT UNDESIRABLE, GIVEN THE HUNDREDS OF THOUSANDS OF EXPENSIVE AND STILL UNOCCUPIED DWELLING UNITS PRODUCED IN THE RECENT PAST. THE CHANCELLOR'S PUBLISHED INTERVIEW WAS PRECEDED BY A WEEKEND STATEMENT BY THE ECONOMICS MINISTER THAT THE TIME TO STEP ON THE ACCELERATOR HAS NOT YET COME.

6. THE GOVERNMENT'S STANCE APPEARS TO BE ESSENTIALLY BACKED BY THE GERMAN ECONOMIC RESEARCH INSTITUTES. ACCORDING TO A SURVEY BY HANDELSBLATT PUBLISHED IN ITS AUGUST 20 ISSUE, ONE OF THE SEVEN INSTITUTES QUESTIONED SUGGESTED THAT A LIMITED RELAXATION OF THE TIGHT REINS MAY BE DESIRABLE, TWO OTHERS ADVOCATED SUPPORT FOR SPECIFIC INDUSTRIES, PARTICULARLY THE BUILDING TRADE, BUT NONE OF THEM SAW ANY NEED FOR IMMEDIATE GENERAL STIMULATION.

7. NOTWITHSTANDING THE PLEDGE OF CONTINUED ADHERENCE TO THE ANTI-INFLATIONARY COURSE IN THE IMMEDIATE FUTURE, EXISTING CONTINGENCY PLANS TO BOOST THE ECONOMY ARE BEING SCRUTINIZED AND FIRMED UP. THE CHANCELLOR TOLD DER SPIEGEL THAT A POTENTIAL LET UP OF FOREIGN DEMAND WOULD HAVE TO BE PARTIALLY OFFSET BY ADDITIONAL DOMESTIC DEMAND VIA SO-CALLED "SCHUBLADEN PROGRAMS" (PROGRAMS NOW IN THE DRAWER), BUT ADDED THAT THE TIME TO OPEN THE DRAWERS HAS NOT COME AS YET. MEANWHILE, HOWEVER, FINANCE MINISTER APEL ANNOUNCED THAT A NEW ECONOMIC PROGRAM "WELL WORTH SEEING" WILL BE DISCUSSED IN HIS MINISTRY DURING THE NEXT TWO WEEKS AND PRESENTED TO THE CABINET UPON THE CHANCELLOR'S RETURN FROM HIS SUMMER VACATION. THIS ANNOUNCEMENT HAS GIVEN RISE TO SPECULATION THAT

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EXPANSIONARY MEASURES MAY BE CLOSER THAN THE CHANCELLOR'S REMARKS MIGHT INDICATE.



8. ACCORDING TO VARIOUS PRESS REPORTS, SOME OF THE INDIVIDUAL GERMAN STATES HAVE ALSO WORKED OUT CONTINGENCY PLANS OR ARE IN THE PROCESS OF DOING SO, WITH THE EMPHASIS REPORTEDLY ON SELECTIVE MEASURES TO SUPPORT CONSTRUCTION, THE AUTOMOBILE INDUSTRY AND MEDIUM AND SMALL-SIZED BUSINESS.

9. AT THE END OF JULY, FEDERAL AND STATE COUNTER-CYCLICAL RESERVES HELD WITH THE BUNDESBANK TOTALED DM 10 1/2 BILLION (FEDERAL GOVERNMENT, DM 7 BILLION; STATES, DM 3.5 BILLION). DM 3.5 BILLION OF THE FEDERAL FUNDS (DM 1 BILLION VOLUNTARY RESERVES AND DM 2.5 BILLION IN RECEIPTS FROM A FEDERAL GOVERNMENT STABILIZATION LOAN) WOULD BE AVAILABLE IMMEDIATELY FOR A POTENTIAL EXPANSIONARY PROGRAM AND RELEASE WOULD REQUIRE ONLY APPROVAL OF THE FEDERAL GOVERNMENT. SOME DM 3.7 BILLION (DM 2.0 BILLION FEDERAL RESERVES AND DM 1.7 BILLION RESERVES OF THE STATES) ARE SUBJECT TO PROVISIONS OF THE STABILITY AND GROWTH LAW, WHICH STIPULATES THAT RELEASE IS PERMISSIBLE ONLY TO WARD OFF A SERIOUS ECONOMIC SLUMP. THE UTILIZATION OF THESE FUNDS WOULD REQUIRE A GOVERNMENT DECREE APPROVED BY THE BUNDESRAT. THE RELEASE OF THE REMAINING DM 3.3 BILLION (FEDERAL GOVERNMENT, DM 1.5 BILLION; STATES, DM 1.8 BILLION) REQUIRES SPECIAL LEGISLATION AND APPROVAL BY BOTH HOUSES.  
CASH

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## Message Attributes

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